

2015

Real Estate Transactions: Cases and Materials on Land Transfer, Development and Finance, 6th Ed.

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REAL ESTATE TRANSACTIONS

CASES AND MATERIALS ON
LAND TRANSFER, DEVELOPMENT
AND FINANCE

SIXTH EDITION

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PAUL GOLDSTEIN

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REAL ESTATE TRANSACTIONS

CASES AND MATERIALS ON LAND TRANSFER, DEVELOPMENT AND FINANCE

SIXTH EDITION

by

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© 2015 LEG, Inc. d/b/a West Academic

444 Cedar Street, Suite 700

St. Paul, MN 55101

1-877-888-1330

Printed in the United States of America

ISBN: 978-1-60930-220-7

Mat #41337345

*To David,
Ethan, Ellie, Gabriel and Benjamin,
Margaret and Matt,
and, especially, Alice*

G.K.

To Jan
P.G.

PREFACE

American real estate practice over the past thirty-five years has been marked by significant changes. The U.S. mortgage finance crisis beginning in 2008 and its aftermath triggered the largest upheaval in residential and commercial mortgage loans since the Great Depression, and its effect on business and legal structures continues to evolve. What began as a cataclysm in the secondary market for American home mortgages became a global financial crisis because many lenders held secondary market securities or had issued "credit default swaps" that effectively made them insurers of the securities. When the value of the securities dropped, the closely tied financial system was on the brink.

The 2008 financial crisis was emblematic of one of the key changes in U.S. real estate transactions over recent decades--a move in many areas towards nationalization and uniformity in what is technically an area of the law within the purview of state regulation. For example, the growth of title insurance has increased the security and efficiency of real estate transactions and contributed to the evolution of a national market for real estate finance. Because title policies are backed by large, resourceful institutions and generally follow nationally uniform standards, title insurance has drawn major institutional lenders and sophisticated financing schemes into every corner of the country. The federal government, the secondary mortgage market, and securitization of mortgage debt have played an increasingly important role in nationalizing and systematizing real estate finance; form mortgage documents promulgated and required by national lenders and insurers are increasingly replacing local finance documents. Enhanced federal and state environmental regulation influences virtually every real estate sale, exposing the parties to potentially devastating liability; public sector incentives as well as private commitment have led to green building initiatives across the country. The civil rights and consumer movements have also left their mark, principally on residential real estate sales. Globalization has increasingly affected American real estate transactions, as U.S. companies expand abroad and U.S. real estate debt is held by non-U.S. entities and individuals. Technology and new service providers across the country have brought competition and commoditization of aspects of work, resulting in changes in how lawyers represent clients in transactions.

The 2008 mortgage crisis was triggered by a combination of various factors: the value of residential mortgage-backed securities in the secondary market crashed, due to speculative lending practices, an unmanaged subprime market, and the bursting of the bubble of an overheated property market. The secondary market essentially collapsed and as of today has only partially rebounded. Federal agencies are still grappling with implementing rules to prevent risky lending behavior and defining permitted credit default swaps for the future. Various agencies have recently settled actions with lenders packaged and sold misleading mortgage-backed securities, with more likely to come. Fannie Mae and Freddie Mac, quasi-governmental agencies that insured home mortgages and facilitated the secondary market, were placed into conservatorship by the federal government because of

looming liabilities; their future has not yet been resolved. The story of the secondary market continues to evolve.

As the mortgage crisis spread into a larger financial crisis, borrowers defaulted on home mortgages when they lost their jobs. Often the values of their homes sank below the amounts they still owed on their loans. This led to widespread foreclosures. The foreclosures spawned significant litigation attempting to unwind assignments of mortgages from secondary market transactions and to determine whether the party bringing foreclosure truly had standing under centuries old doctrines. There was a spate of lender misbehavior in some of the foreclosure activities as well, triggering equitable relief and consumer law actions. Federal and state legislation was passed to assist troubled borrowers, including loan modification programs. While the number of foreclosure actions has decreased as of this writing, troubled borrowers remain and the residential real estate markets in many areas remain well below their 2008 levels. This too is a real estate story that continues to unfold.

Some of the recent changes in real estate transactions, such as the spread of title insurance, have taken work away from lawyers. Other changes, because they implicate a wide and complex range of legal issues, have magnified and complicated the real estate lawyer's role. It is no longer sufficient to know the law on title conveyancing and mortgages. The real estate lawyer today must also grasp at least the basics of federal income taxation, personal property security, environmental regulation, bankruptcy, and products liability law. After the 2008 financial crash, the real estate lawyer will also need to understand federal and state lending and consumer credit regulation and ongoing changes in that law. The attorney must also have a feel for the informal legal culture created by the many nongovernmental institutions and individuals involved in real estate transactions—brokers, title companies, surveyors, appraisers, lenders and their various trade associations.

And yet, despite the rise and effect of new forces, real estate practice still requires a firm grounding in fundamental concepts such as real estate contracts, mortgages and foreclosure, title systems, and brokerage. These are the vocabulary and the grammar of the sophisticated real estate lawyer. New judicial decisions, legislation, business practices, and transaction structures that respond to emerging economic and social demands are built on this foundation. For example, court opinions and legislative debate on the proper response to the post-2008 foreclosure crisis almost always have been framed within the context of applying or changing longstanding doctrines in order to achieve a desired result; alternative financing vehicles designed by lenders have been based on past precedent and practices.

The essential role of the real estate lawyer has also not altered over the years. This book continues to frame issues from the perspective of a lawyer assembling a successful transaction and not simply litigating a deal gone bad. The task of the transactional lawyer requires great sophistication, wisdom, and at times subtlety. All parties in a deal want

it to close, and according to the economists each should be in a better position if it does. Each party, however, wants to obtain as great of an advantage as possible. The skilled transactional lawyer will advance the client's interest but also will ensure that the interests of all parties are aligned (or else the transaction ultimately will fail), the parties don't walk away from the deal, and the long term relationship between the parties remains intact.

This book, therefore, encompasses emerging, as well as traditional, fields of real estate law. Part One covers the basic elements of real estate transactions, using the residential transaction and as-built commercial transaction as a vehicle for exposing the fundamentals of the role of the attorney, brokers, real estate contracts and conveyancing, title assurance, and secured financing. Part Two covers commercial real estate transactions, exploring contemporary innovations in financing and leasing techniques and examining current issues related to distressed properties, environmental regulation and green buildings, globalization of real estate transactions, and the development and operation of shopping centers. Part Three presents all tax materials, including residential and commercial issues.

Although real estate transactions have become increasingly subject to nationalizing influences, real estate law remains in many respects the creature of local rules. As a consequence, one message should be emphasized here: no real estate lawyer can safely ignore applicable state law when counseling on any transaction, large or small.

Real estate law is a happy blend of practical insight and academic perspective, a mix that we have tried to convey in the pages that follow. Colleagues in practice and in academe have provided helpful comments for the preparation of various editions of this book. We are particularly grateful to Todd Davis and Jonathan Adler for their help with the environmental law materials, Edward Hurtuk, Charles Daroff and Zachary Paris for their insights on new developments in real estate law, Andy Morriss for his ideas on many subjects, Leon Cabinet for his comments on the tax materials, and Hiram Chodosh and Erik Jensen for insights on globalization issues. We also appreciate Kevin McMunigal's and Bob Lawry's comments on professional responsibility issues, Morris Shanker's comments on bankruptcy, and Bill Warren's ideas on shopping centers. Last but not least, Jim Hagy has been a generous and terrific source of wisdom on real estate law, lawyering, and pedagogy.

Many law teachers who used various editions of this casebook have been generous with their suggestions. For their thoughtful comments, we are indebted to Professors Steven B. Baslaw, J. Wendell Bayles, Roger Bernhardt, Zareh H. Beylerian, William M. Blackburn, Michael Braunstein, Pamela W. Bray, John D. Briggs II, D. Barlow Burke, Jr., K.C. Collette, John W. Fisher II, Robert L. Flores, Ken Harmon, Theodore B. Hertel, Jr., John F. Hicks, Alex Johnson, John W. Larson, Carl H. Lisman, Ward F. McDonald, George K. Miller, Thomas Mitchell, C. Robert Morris, Phillip J. Nexon, Lindsay F. Nielsen, John R. Nolon, Georgette Chapman Poindexter, Patrick A. Randolph, Jr.,

Robert S. Rollinger, Peter W. Salsich, Jr., M. John Schubert, John M. Tyson, G. Graham Waite, Robert Weiler and Alan M. Weinberger.

A Note on Style. Most of the cases and other materials appearing in these pages have been edited. The deletion of sentences and paragraphs is indicated by ellipses; the deletion of citations is not indicated. Most footnotes have been excised. The remaining footnotes retain their original numbering. Authors' footnotes are lettered.

G.K.

P.G.

New York, New York
Stanford, California
September, 2014

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